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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 889

ESTATE OF R. A. SEWELL, JOSEPHINE M. SEWELL,
EXECUTRIX,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

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COMMISSIONER OF INTERNAL REVENUE, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The Estate of R. A. Sewell, Josephine M. Sewell, Executrix, respectfully prays for a writ of certiorari to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit, entered in the above-entitled cause, and denying her petition for a rehearing, filed in said cause.

Judgment and Opinion Below

The judgment of the Circuit Court of Appeals for the Fifth Circuit was entered on November 9, 1945 (Record 206-209), and its opinion on that date is reported in the Advanced

Sheets of the Federal Reporter, *Sewell's Estate* v. *Commissioner*, 151 F. (2d) 806 (No. 12, January 14, 1946). The judgment below affirms the decision of the Tax Court of the United States (R. 34-78, 84), which has not been reported.

Jurisdiction

The judgment of the Circuit Court of Appeals for the Fifth Circuit was entered on November 9, 1945 (R. 209). Petitioner filed her petition for rehearing on November 29, 1945 (R. 210). The Circuit Court of Appeals entered its order and judgment denying such petition for rehearing on December 28, 1945 (R. 218). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A. Sec. 347).

Statement of the Case

This case involves alleged errors in income tax deficiencies for the years 1934, 1935, 1936, and 1937, imposed upon R. A. Sewell and his Estate (after his death in 1940) (R. 5-20). The basic issues controlling taxability of dividends, profits from sales and pledges, and interest on proceeds therefrom, against Sewell during the first three of those years, concern the completeness and validity, for Federal income tax purposes, of his alleged gift, on January 2, 1934, to his wife, Josephine M. Sewell (Petitioner as Executrix), of 1,000 shares of corporate stock in Sewell Manufacturing Company, a Georgia corporation, and both parties being residents of Georgia, and of 300 additional shares of that Company in July, 1936; all of which shares, without physical delivery of the certificates to her, were, under the practice of the Company to retain stockholders' certificates in its Stock Book, transferred to her on the books of the corporation, the old certificates being marked "Canceled," and the new ones issued in her name, with other facts as hereafter

indicated. The other basic issue concerns the existence of an alleged partnership during 1936 and 1937, or either year, between R. A. Sewell and Josephine M. Sewell, with their four minor children added as special partners from July 1, 1937, on which depends the taxability of profits of the business conducted under the name of Sewell Hat Manufacturing Company and Sewell Hats. The necessary facts on the legal questions involved are indicated therein, and for a clearer understanding of the case are stated with more detail in the supporting Brief.

Two other cases—*W. P. Sewell* v. *Commissioner of Internal Revenue* and *R. B. Sewell* v. *Commissioner*—were, for convenience in taking evidence, heard by the Tax Court with this case, and it was agreed that any evidence in one case could be considered in any other so far as pertinent therein; but there was never any consolidation of this case with the others (R. 103, 152, 34, 84, 206, 209, 218). All involved gifts of stock in the same Company, but the facts as to dominion and control, and sales and pledges of the stock by the present donee, were essentially different; and the present case alone involved questions of partnership.

The Tax Court ruled adversely to Petitioner as to each of the basic issues and the legal questions next stated; and the Circuit Court of Appeals affirmed its decision thereon. (R. 34-52, 55-71, 76-78—omitting references to other petitioners; 206-209, 218.)

The Questions Presented, and Specification of Errors

1. Where the formalities of local law, under statutes and appellate decisions of the State of the property transactions, are observed in the making of gifts of corporate stock, and in the formation of a partnership thereafter between the donor and donee, a husband and wife, and there is no fraud or sham designed to evade Federal income

taxes, and the gifts and the partnership each are manifested, orally and in writings, by actual overt acts of the parties which are sufficient under such local law to render each transaction complete and valid under that law—can the Tax Court of the United States, and a United States Circuit Court of Appeals on a petition by the taxpayer to review the decision of the Tax Court, properly fail to give effect to such local law, either as to gift or as to partnership, in a controversy between the husband (and his estate after his death) and the Commissioner of Internal Revenue as to Federal income taxes, alleged tax deficiencies on income and profits from the alleged gifts or their proceeds and on profits of the alleged partnership, under the Commissioner's contention that there was neither any complete or valid gift, nor any valid partnership, for Federal inome tax purposes, and therefore the husband and his estate are liable for all such income and profits? The Circuit Court of Appeals and the Tax Court of the United Stats each erred in failing to apply such controlling local law to each of such transactions, especially where the Tax Court found that there were no fraud and no "shams designed to evade tax."

2. Where, at the time of an alleged gift of shares of corporate stock, there is no express agreement or understanding between an alleged donor and donee (a husband and wife) that the husband shall retain dominion and control over the gift stock or income or proceeds therefrom, and the husband never asserts any dominion or control over the stock itself, and his only exercise, if any, of dominion or control over the subject-matter of the alleged gift is that, more than sixteen months after the alleged gift and subsequently, he uses proceeds therefrom to build and equip a manufacturing plant and operate the same, and where (after the husband's death), in a controversy

between the Commissioner and the wife (as executrix of the husband's estate) as to liability for Federal income taxes on income, profits, and interest from the subject-matter of the alleged gift or its proceeds, the wife claims that such uses by the husband of such monies were under a loan from her for uses other than by gift from her to him, and there is nothing to evidence any such gift by her to him of either the subject-matter of the gift or its proceeds, or as to any *consent* by her to such uses other than by loan to him of such monies—would the mere fact of such uses by him of the monies, sixteen months after the alleged gift and subsequently, be significant or pertinent to manifest and establish a lack of donative intent in the making of such alleged gift, and thus invalidate the gift? The decisions of the United States Circuit Court of Appeals and of the Tax Court were based primarily on the holding, as to this Petitioner, that such long subsequent uses sufficed to manifest an absence of essential donative intent in the making of the two alleged stock gifts, and therefore they were incomplete and invalid; and such holdings being based on an erroneous rule of law in testing the validity of a gift, each Court erred therein, and in failing to apply the correct rule that such uses long after the gifts were not pertinent or significant to show invalidity of the gifts.

3. Where gifts of corporate stock from a husband to a wife are made by transfer on the books of the Company, the original certificates being marked "Canceled," and new certificates being properly issued with her name therein, which, according to the practice of the Company and its stockholders (consisting both of brothers of the husband and of others), remain in the Stock Book in its vault in the custody of its secretary and treasurer (not a family stockholder) in its vault at its offices, accessible at any time to the wife, and where, under the law of the State, such

transfers, with the undisputed acts of the parties, would be sufficient to constitute complete and valid gifts—would the mere fact that the parties are husband and wife, and that, more than sixteen months after the alleged gift and subsequently, the husband uses proceeds from such stock in building and equipping a manufacturing plant and starting the operation of such business, nullify the alleged gifts for Federal income tax purposes under Sections 11, 12, and 22 (a) of the Revenue Act of 1934, c. 277, 48 Stat. 680, and identical provisions under those numbers in the Revenue Act of 1936, c. 690, 49 Stat. 1648 (subsequent Revenue Acts containing identical provisions)—the statutes in force at the time of the transactions in question—or nullify the alleged gifts by any applicable Federal legal rule, under the Revenue statutes, controlling such transactions? The Circuit Court of Appeals and the Tax Court each erred in misconstruing the proper rule of law in such a case, and in thus holding that the gifts were incomplete and invalid for lack of donative intent because of dominion and control of the donor (exercised only by long-subsequent uses of the proceeds, as stated, which did not constitute dominion and control over the gift within the meaning of the law of gifts or the Federal income tax statutes).

4. Where, under the laws of Georgia (the State of residence of the parties and of the transactions in question) effective at the time of the transactions, a gift is valid if there is an intention by the donor to give, acceptance by the donee, and delivery of the article given or some act accepted by the law in lieu thereof, and if the donation is of substantial benefit, acceptance is presumed unless the contrary is shown, and where under such local law an actual manual delivery is not essential to the validity of a gift, but a constructive or symbolic delivery, manifested by the donor's relinquishment of dominion and control and

by the donee's exercise thereof, suffices, and where there are neither fraud nor "shams designed to evade tax" in the transactions in question—does the owner of stock in a Georgia corporation sufficiently express and establish donative intent, essential for a valid gift, and complete and effect a valid gift to his wife of shares of such stock, where, before and at the time of such transfer, he informs her, the corporate officers, and other persons of his intention to give her such stock, and by his direction the certificates for such shares standing in his name on the Company's Stock Book are marked "Canceled," and new certificates for such shares, sealed and signed by the proper corporate officers, are issued in her name, which certificates are not manually delivered to her, but, according to the practice of the Company and other stockholders as to holdings and dealings in stock, remain in the Company's Stock Certificate Book undetached therefrom, in the custody of its secretary and treasurer in the vault of its office, open and accessible to stockholders and with access of the wife to such book and certificates at any time; and where she does not indorse such certificates at the time of their issuance to her or until about the time of her sale of part of such stock to other persons, the first between eleven and twelve months after the alleged gift, and other sales seventeen, twenty, twenty-one, thirty-four, and forty-six months after such alleged gift; and where the wife herself also executes valid, unquestioned pledge contracts to other persons, pledging more than one-fourth of such stock as security for loans to her, after the alleged gift, which instruments are signed by herself as pledgor and by the pledgees, attested, and recorded in the public records, and the wife also later exercises the option given her by the pledge contracts to surrender the stock to the pledgees instead of paying the loans; and where the husband makes to the Government income tax authorities sworn Gift Tax Re-

turns as donor, showing the gifts of stock to the wife, and the wife attaches to such returns her signed acknowledgments as to the making of such gifts, and the husband pays the gift taxes assessed thereon; and where both, by separate Individual Income Tax Returns after the alleged gifts, report to the Government tax authorities the dividends, interest, and profits from said sales and pledges of stock, only as accruing from shares of stock and monies belonging to the wife, and she pays the income taxes thereon; such transactions being during the years from 1934 to 1937 inclusive? The Circuit Court of Appeals and the Tax Court erred in holding that such transfers of stock and acts did not constitute complete and valid gifts as to each of such years; and in failing to give effect to the correct rule of law that such transfers on the corporate books and acts were sufficient.

5. Where an alleged gift of corporate stock, such as stated in the preceding questions, is made by a husband to his wife in a January (1934), and during that tax year dividends accrue with profits therefrom, which monies, according to the practice of the Company with all its stockholders to act for them practically as a bank by allowing accounts on its books with credit and debit entries, are so credited to the wife's separate account on its books, and such monies so remain in such account throughout the same calendar year (1934) without any withdrawal or use by her or the husband during that year and early in the next year (1935) the husband makes to the Government tax authorities a Gift Tax Return showing such stock as given to the wife, to which Return she attaches her own signed Donee's Information Return certifying the correctness of such gift, and the husband pays the Gift Taxes thereon as assessed by the tax authorities; and also, early in the year (1935) after that of such alleged gift and such accrual of monies

and credit thereof to the wife's account, she makes her Individual Income Tax Return to the Government tax authorities, returning and paying income taxes on such dividends as accruing and credited to her in the preceding year (1934), and the husband does not include the same in his Individual Income Tax Return for that year (1934)—would the fact that, after all such returns, and after more than sixteen months subsequent to the alleged stock gift, the monies above stated as accruing during the preceding year (1934) are transferred from the wife's account to the husband's account on the Company's books, and he then uses such monies, render him (or his estate after his death) liable for Federal income taxes on such dividends and profits from a sale, accruing and credited to the wife during the preceding tax year (1934), so as to render the husband liable for *taxes on such previous year's dividends and profits,* instead of the wife *for that year,* in the absence of any fraud or shams designed to evade tax? The Circuit Court of Appeals and the Tax Court erred, by application of erroneous rules of law, in holding the husband (and his estate) liable for such 1934 taxes.

6. Where, under the laws of Georgia (embodied in its statutes and appellate court decisions), effective at the time of the transactions in this State, a partnership may be created by oral contract, or may arise from a joint ownership, use, and enjoyment of the profits of undivided property, real or personal, and where, unless otherwise provided by agreement, partners are made by such local law equally interested in all the stock or property brought into the business, it matters not by which partner, and are made equally entitled to share the profits and equally bound to pay the losses, and a married woman may lawfully be a member of a partnership with her husband, and is entitled to an accounting for her share of the profits,

although she has not managed or actively participated in the business; and where a husband and wife, for the carrying on of a hat manufacturing business (not of the personal-service or technical-expert class), orally agree that she shall be a partner therein, on account of her having contributed and the husband having used, in building and equipping such plant, monies derived from corporate stock, under his alleged gift to her more than two years before, and where there are no other persons as partners at the time of formation of such alleged partnership (in 1936), and where (after several months' operation in the business by the husband's brother during the husband's illness, in late 1935 and early 1936, and receipt by the husband of a deed back to the plant and business), the business is then operated under a trade name, and the husband informs other persons that such a partnership exists, and at the close of business (December 31, 1936) book entries are made showing such a partnership and the interests of the partners, and there are no fraud or shams designed to evade tax in the transactions, and the business thus continues during the next year (1937)—do such oral partnership agreement and operation of the business constitute a valid partnership, for Federal income tax purposes, as to either of such years, even though the husband, by the wife's agreement or consent, actually manages the business in both years, and she takes no active part therein otherwise than with respect to the capital as stated? The Court of Appeals and the Tax Court erred in holding adversely to Petitioner as to such matters, by erroneously holding that the husband had made no valid gift to his wife (under errors of law as above indicated), and that she had made no contribution to the capital (under such errors and the error indicated in this question), and in holding erroneously, as a matter of law, that the wife's lack of active participation in the business was fatal to a partnership.

7. Where the law of the State of the transactions, at the time thereof, exists as stated in the preceding question, and the parties act as therein stated—can the existence of such a partnership be nullified or ignored, for Federal income tax purposes, for the reasons assigned by the Tax Court of the United States, and the Circuit Court of Appeals for the Fifth Circuit by affirming such decisions: that the two-year-previous alleged gift of corporate stock by the husband to the wife was invalid for lack of donative intent, by reason of the husband's retention and exercise of dominion and control over such stock; that (as Petitioner, executrix of her husband's estate) she relied on a "*purchase*" of her interest in the alleged partnership, and not on a "*gift*" from her husband of such partnership interest; and hence, since the original stock gift was invalid, she had not "*purchased*" such an interest, that she had nothing to give to her children (who were given small interests in the alleged partnership, first orally and last in June or July 1937 by a written trust agreement and a limited partnership agreement signed by the husband and wife as individuals and as trustees); and that,—notwithstanding the oral 1936 agreement, and the 1937 written agreements making the husband alone the general partner, who alone under the Georgia law of limited partnerships could manage the business and act for the partnership—there was no sort of partnership during either 1936 or 1937? The Circuit Court of Appeals and the Tax Court erred in so holding, and their rulings were based upon such manifest errors of law, in contravention of the undisputed facts; the record merely showing a recital in such 1937 trust agreement that Josephine M. Sewell had "purchased and paid for" an interest in such hat manufacturing business (which, if not accomplished by the validity of the previous gift, at least operated as a gift, of such interest, provided there was no implied trust under

the rule of the Georgia Supreme Court, that a use by a husband of his wife's monies creates such a trust); and the record wholly failing to show that Petitioner, in contending that a partnership existed in both 1936 and 1937, limited her reliance to a "purchase" or to any specific basis in acquiring her interest.

8. Where the laws of Georgia, the State of the transaction involved, then and since have recognized the validity of general partnerships created by oral agreement, and have made such partners *equally* entitled to share in the profits and losses of the business, although the wife does not actively participate therein, and have recognized the validity of limited partnership agreements, created in writing and giving only the general partner a right to manage the business, and have recognized the validity of trusts for minor children, and where in June or July of the last year indicated in the preceding question (1937) the husband and wife executed such a limited partnership agreement and such a trust agreement (by which their four minor children received first a 20 percent interest and later a 33⅓ per cent interest in the partnership and assets of the business), and only the husband was made the general partner (with the right of management as provided by statute), and where the statutory formalities as to limited partnerships were complied with, and no attack has been made upon the validity of such trust and limited partnership instruments (other than to insist that the former was not executed until the middle of 1937, which Petitioner concedes), and where the parties conducted the hat manufacturing business during 1936 and 1937 as stated in this and the two immediately preceding questions, and the husband for both of such years made to the Government tax authorities Partnership Income Tax Returns, showing a partnership with interests as above stated, and the hus-

band and the wife in their separate Individual Income Tax Returns for those years returned the profits from such business according to the partnership status and interests in them as above stated, and paid their income taxes accordingly, besides making Gift Tax Returns as to their children with respect to the interests given them; and where the parties in each of such years have acted upon the assumption that such partnership and partnership interests existed, and in 1938 executed to the Reconstruction Finance Corporation a security deed to the assets of the business, signing as a partnership, and where there were no fraud or shams to evade tax in such transactions—could the Circuit Court of Appeals and Tax Court of the United States legally or properly fail to apply the local law as to the validity of such a general partnership in 1936, or, limited partnership in 1937 (the tax years involved), or properly fail to apply the definition by this Court of a partnership, made in *Meehan* v. *Valentine,* 145 U. S. 618, in consonance with the local law, or properly base their holdings on erroneous rules of law and incorrect legal standards, above stated, as to what constitutes a valid partnership for Federal income tax purposes? The Tax Court erred in so holding as to each of the years 1936 and 1937, as well as in holding that the alleged stock gifts in 1934 and 1936 were invalid; and the Court of Appeals erred in affirming such holdings and decisions, for the reasons stated.

9. Petitioner (to comply with the Rules of this Court) also assigns error on the refusal of the Circuit Court of Appeals and the Tax Court to grant redeterminations of the alleged income tax deficiencies in each of the years 1934, 1935, 1936, and 1937, for each of the reasons above stated; and urges that each adverse holding complained of is without substantial evidence to support it, if the correct legal rules and standards as to gifts and partner-

ships, as stated in this petition, are given effect, and that the adverse holdings of the Tax Court are without legal warrant in the record; and therefore that the Court of Appeals erred in affirming such holdings and decision.

Reasons for Granting the Writ

1. The decision of the Circuit Court of Appeals for the Fifth Circuit is in conflict with the decisions of other Circuit Courts of Appeals on the same matter, in the law of *gifts,* and in such law for Federal income tax purposes; in that the Court below, in affirming the holdings of the Tax Court, held that the alleged gifts of corporate stock—though made by transfers on the corporate books, the cancellation of the donor's certificates, the issuance of new certificates therefor to the donee, and with Gift Tax Returns, and acknowledgments of the donee, made by the donor to the Government tax authorities, and other acts of the parties as stated—were invalid for lack of donative intent and for continued exercise by the donor of dominion and control over the stock, for the sole reasons that there was no physical delivery of the stock certificates to the donee, and that, more than sixteen months after the transfer and subsequently, the donee used dividends and other proceeds from the stock. Such decision directly conflicts with two decisions of the Circuit Court of Appeals for the Sixth Circuit, *Marshall* v. *Commissioner,* 57 F. (2d) 633, and *Bardach* v. *Commissioner,* 90 F. (2d) 323; each holding, in Federal income tax cases, that such a transfer on the books of a corporation from a husband to his wife, constitutes in itself a delivery, vests legal title to the transferred stock in the wife; and that subsequent use by the husband of dividends or proceeds from the stock are without effect to invalidate the gift, since what the wife does with her monies after the gift is "a matter of com-

plete indifference." The present decision also conflicts with those of the Circuit Court of Appeals for the Eighth Circuit in *Edson* v. *Lucas,* 40 F. (2d) 398, 406, and *Mahaffey* v. *Commissioner,* 140 F. (2d) 879, 882; the former involving a gift of stock in trust with the question of bona fides, and holding that "The gift, if completed at all, was completed in 1919, and what (the alleged donor) did with the proceeds of the stock in 1920 could not defeat it;" and the latter holding that "The subsequent transactions of petitioner with reference to the stock transferred in trust are without significance." The instant decision is further contrary to the decision of the Circuit Court of Appeals for the Second Circuit in *Guaranty Trust Co.* v. *Commissioner,* 98 F. (2d) 62, to the effect that, where a question of collateral agreement or condition as to the loan of identical amounts of money back to the donor was involved, this could be shown by proof that there was "no clear separation of the discussion culminating in the alleged gift and the discussion about setting up the trusts and lending the money back to the husband * * * made that evening," all the steps following "one another closely and the entire transaction (being) agreed upon," and the trust deed "executed the day following the conversation;" but that, if the gifts "were completed before the agreements that the money should be loaned," the transaction was valid. The present decision is also contrary to that of the last-named Circuit Court of Appeals in *Richardson* v. *Smith,* 102 F. (2d) 697, where, unlike the present case (where the Tax Court held that there were "no shams designed to evade tax"), the question arose as to whether there was "a sham" in an alleged gift by husband to wife, and it was held that "a series of transactions," in all of which the wife might have yielded to her husband's will, all *practically contemporaneous* with the gift in question, could be considered on the question of donative intent,

dominion and control, or agreement or understanding between the parties at the time of the alleged gift; but that a mere expectation or hope of the donor, at the time of the transaction, that he will receive benefits from the subject-matter of the gift is insufficient; and the case was remanded for reconsideration of the facts in the light of the correct rule of law.

2. The decision of the Circuit Court of Appeals for the Fifth Circuit, in nullifying the transactions here involved—although, as the Tax Court itself found, there were no fraud and no "shams designed to evade tax," and although the uncontroverted facts showed that the transactions were actualities and not fictions—also conflicts with decisions of the Circuit Court of Appeals for the Eighth Circuit in *Fordyce* v. *Helvering,* 78 F. (2d) 525, following earlier decisions by the instant appellate court itself in *Saenger* v. *Commissioner,* 69 F. (2d) 631, and *Planters Cotton Oil Co.* v. *Hopkins,* 53 F. (2d) 825, that "fraudulent pretense absent, the Government accepts the taxpayer as it represents itself to be, and it must make its returns and pay its taxes accordingly." The present decision on the same matter also conflicts with those of the Circuit Court of Appeals for the Second Circuit in *Johnson* v. *Commissioner,* 86 F. (2d) 710, that "legal transactions cannot be upset merely because the parties have entered into them for the purpose of minimizing or avoiding taxes which might otherwise accrue;" and *Chisholm* v. *Commissioner,* 79 F. (2d) 14 (101 A. L. R. 200, 204), that a tax-saving object "is, of itself, no reason for non-recognition of the transaction, if it was *real and not illusory.* Mere purpose to avoid tax does not in itself vitiate a transaction." (All italics ours.)

3. The decision of the Circuit Court of Appeals in this case—by affirming the decision and holding of the Tax

Court that no partnership existed, not only because as held the wife contributed nothing to the capital of the business, but because the husband managed the business and she took no active part therein, and, in effect, that such an active participation by her was necessary to a valid partnership for Federal income tax purposes—also is in conflict with the decisions of two other Circuit Courts of Appeals to the contrary, holding in effect that (in businesses not essentially of the personal-service or technical-skill type), a material contribution to capital alone is sufficient—by the Circuit Court of Appeals for the Tenth Circuit in *Champlin* v. *Commissioner,* 71 F. (2d) 23, 26; and the Circuit Court of Appeals for the Sixth Circuit in *Rose* v. *Commissioner,* 65 F. (2d) 616.

4. The Circuit Court of Appeals in this case has also decided Federal questions in a way probably in conflict with applicable decisions of this Court; such questions involving the validity of gift and partnership transactions under a proper recognition of the correct legal rules as to the taxability of income from such alleged gift property and from profits of such alleged partnership, under the Federal income tax statutes, Sections 11, 12(b), 22(a), 181 and 182 of the Revenue Act of 1934, c. 277, 48 Stat. 680, and identical provisions under those numbers in the Revenue Act of 1936, c. 690, 49 Stat. 1648, and later Revenue Acts (26 U. S. C. A. "Internal Revenue Acts," pp. 665, 669, 728); the first three sections relating to normal tax, surtax, and gross income, and the last sections to partnerships. The decision and holdings in this case that income and profits from the alleged gift properties and the alleged partnership were taxable solely to the donor husband and his estate, and in failing to apply the controlling local law of the State under its highest court decisions as to the validity of such gifts and partnership—notwithstanding the holding of the

Tax Court that there was no fraud, evasion, or sham in such transactions, and the undisputed evidence as to the reality of the transactions, the completeness of the gifts, and the actuality of the partnership—conflicts with decisions of this Court:

(a) In *Gregory* v. *Helvering*, 293 U. S. 465, and *Moline Properties* v. *Commissioner*, 319 U. S. 436, holding in effect that, where there is no fraud or fiction, a mere motive of tax reduction or avoidance will not nullify actual transactions.

(b) In *Meehan* v. *Valentine*, 145 U. S. 618, that "The requisites of a partnership are that the parties have joined together to carry on a trade or adventure for their common benefit, each contributing property *or* services, and having a community of interest in the profits;" thus, in effect holding, contrary to the present decision, but in conformity with Georgia law, that a contribution to capital is sufficient without the rendition of services.

(c) In *Morgan* v. *Commissioner*, 309 U. S. 78, 80, holding that "State law creates legal interest and rights. The Federal Revenue Acts designate what interests or rights so created shall be taxed." In *Blair* v. *Commissioner*, 300 U. S. 5, and *Helvering* v. *Stuart*, 317 U. S. 154, holding that the rules of State law control as to grantees, donees, and others taking under deeds, wills, or trusts. In *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64; *Garrett* v. *Moore-McCormack Co.*, 317 U. S. 239, 245, and *Magnolia Petroleum Co.* v. *Hunt*, 320 U. S. 430, 445, recognizing, as in the preceding cases, the controlling effect of State statutes and appellate decisions on property rights, unless there is a conflicting Federal statute.

5. The Circuit Court of Appeals in this case has also decided important questions of local law in a way probably in conflict with applicable local decisions: (a) As to *gifts*—

in holding in effect that these were not complete or valid in the absence of a manual delivery of the corporate stock certificates to the donee, notwithstanding the uncontroverted facts as to the transfers on the books of the corporation, with formal acceptance by the donee's signed acknowledgments to the Government attached to the donor's Gift Tax Returns, and as to the donee's sole exercise of dominion and control over the stock by sales and written pledges thereof in her own name; such holdings being contrary to the Georgia appellate court decisions construing or under its Code of 1933, Sections 48-101—48-103 and 53-404, in terms dispensing with the necessity of "actual manual delivery" where there has been a "constructive delivery," consisting of any act indicating a renunciation of dominion by the donor and its transfer to the donee, creating a presumption of acceptance by the donee, and permitting transfers of property by husband to wife; such decisions holding that a symbolic delivery will suffice, and "the mere fact that the donee allows possession to remain with the donor will not necessarily defeat a gift" (*Hall* v. *Simmons,* 125 Ga. 801); that, where the conduct of the parties shows a change in the ownership of chattels, a gift is complete without the necessity of an actual delivery (*Poullain* v. *Poullain,* 79 Ga. 11; *Underwood* v. *Underwood,* 43 Ga. App. 645); that "the legal unity of husband and wife has, in Georgia, for most purposes been dissolved, and a legal duality established. A wife is a wife, and not a husband as she was formerly * * * A husband can make a gift to his own wife, although she lives in the house with him and attends to her household duties, as easily as he can make a present to his neighbor's wife." (*McNaught* v. *Anderson,* 78 Ga. 503.)

(b) *As to partnership*—in failing to apply to the uncontroverted facts as to an actual partnership, in each of the

years 1936 and 1937, the controlling rules of local law, in decisions construing or under the Georgia Code of 1933, Section 75-101, that "a partnership may be created by • • • parol contract, or it may arise from a joint ownership, use, and enjoyment of the profits of undivided property, real or personal;" Section 75-206, that "unless otherwise provided in the agreement, partners shall be equally interested in all the stock or property brought into the business, it matters not by which; partners shall be equally entitled to share the profits and equally bound to pay the losses;" and Sections 75-401—75-409 and 75-417, providing for limited partnerships with general and special partners, and authority only for the general partner to manage or act for the partnership; and such decisions holding that an oral partnership agreement is sufficient, even though the nature of the property would otherwise be covered by the statute of frauds (*Lane* v. *Lodge*, 139 Ga. 93(3, b); *Smith* v. *Padrosa*, 139 Ga. 484, 487); that it has been long settled in Georgia, under its Supreme Court cases cited, that "a married woman may contract to become, and actually become, a member of a partnership with her husband, or other persons," and (in a case of general partnership) "it is not necessary to specify as to the liability for the losses in such cases," and the wife is entitled to an accounting for her share of the profits, "though she had *no participation in the active management of the business.*" (All italics ours.) (*Butler* v. *Frank*, 7 Ga. App. 655 (2), 657, 658.)

(c) *As to partnership*—in failing to apply the local rule, laid down by the Supreme Court of Georgia in *Allen* v. *Allen*, 198 Ga. 269(3), that, "Whenever a husband, with or without the wife's consent, acquires from her money which is her separate property, he must be deemed to hold it in trust for her benefit, in the absence of any evidence that she intended to make a gift to him;" so that, if there were

complete, valid gifts by the husband to the wife of the corporate stock here involved, and if the husband used its proceeds either "with or without the wife's consent," without anything to show a "gift" of such proceeds by the wife to the husband, such proceeds constituted an *implied trust* to the wife—irrespective of whether or not she had expressly *loaned* them to the husband, and she could have imposed such trust on the plant and assets of the Sewell Hat Manufacturing Company, unless her husband recognized and protected her rights. He having done so, by orally agreeing that because of such contribution she would be a partner in the business (according to the uncontroverted evidence), her contribution, as a matter of law, afforded full consideration for the partnership agreement, and a contribution (more than half) to the capital. Therefore the holding of the Tax Court that she "*purchased*" no interest in the partnership was erroneous, was contrary to the controlling law of the State in such a case; and the decision of the Court of Appeals in affirming such decision and holding was likewise contrary to such law.

6. The Circuit Court of Appeals in this case has decided important questions of Federal law which have not been, but should be, settled by this Court—not only because of the conflict of this decision with those of other Circuit Courts of Appeals and local decisions on important questions, and a probable conflict with decisions of this Court—but because the particular questions of law here raised have never been decided by this Court, and such a decision is of vast importance—to enunciate and settle the true principles of construction and rules to be applied in Federal income tax cases under the Internal Revenue Statutes as to gifts, partnerships (with the essentials thereof in such cases, as to a contribution of capital and active participation in the business); whether the rules of "economic"

ownership or enjoyment and of dominion and control "for income tax purposes" as between a husband and wife, announced by this Court, apply to ordinary gifts as well as to those in trust, and apply where there is no fraud or sham designed to evade tax, and to what extent local statutes and decisions, which would otherwise control, are applicable, in Federal Income Tax cases, to gifts and partnerships. A decision of such vital questions, on which the Circuit Courts of Appeals and the Tax Court itself (by conflicts in decisions and dissenting opinions) have long been much divided, with confusion in the proper construction and administration of Federal tax law and the application therein of local law, we respectfully submit is vitally important to tax authorities, taxpayers and all attorneys who are constantly called upon to advise them, without certainty as to the correct legal rules, standards, criteria, and tests to be applied in such cases.

While this Court has decided many questions as to trusts under the income tax statutes, and the effect thereon of State laws and decisions, it has made no such decision with regard to other gifts. Nor has this Court made a determination of the questions here involved as to partnerships; *Meehan* v. *Valentine,* 145 U. S. 618, only defining generally the requirements of a partnership, though indicating that either a contribution to capital alone or services will suffice; and *Burnet* v. *Leininger,* 285 U. S. 136 (the only decision relating to partnerships in income tax cases) being inapplicable to the present questions, since the husband there gave to his wife only "a derivative interest" without a transfer of "partnership corpus" (making the rule of *Lucas* v. *Earl,* 281 U. S. 111, controlling), and other partners did not consent to the wife's becoming a member of the partnership.

Statutes Involved

The Federal Statutes involved are Sections 11, 12 (b), 22 (a), 181, 182, and 801 (a) (3) of the Revenue Act of 1934, c. 277, 48 Stat. 680, and identical provisions with corresponding numbers in the Revenue Act of 1936, c. 690, 49 Stat. 1648, except that the last-stated section is numbered 1001 (a) (3), these provisions appearing also in subsequent Revenue Acts (26 U. S. C. A., "Internal Revenue" and "Internal Revenue Acts 1924 to Date"). The local statutes involved are Sections 48-101, 48-103, 53-404, 75-101, 75-206, 75-401, 75-406, 75-409, 75-417, and 108-114 of the Georgia Code of 1933. These Federal and State statutes are set forth in the *Appendix* after the Brief in support of this Petition.

Wherefore your Petitioner, referring to the attached Brief in support of the foregoing reasons for review, respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Fifth Circuit, commanding that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in this case; and that the said judgment and decision of the United States Circuit Court of Appeals for the Fifth Circuit may be reversed by this Honorable Court; and that your Petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 889

ESTATE OF R. A. SEWELL, JOSEPHINE M. SEWELL, EXECUTRIX,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

BRIEF IN SUPPORT OF PETITION

At regrettable though unavoidable length, but we trust without prolixity in view of the many conflicting decisions and important questions involved, we have endeavored to state such questions and reasons for granting the writ of certiorari with sufficient clarity and fullness to give this Court a clear picture of the situation, in respectfully appealing to its discretion for the grant of the writ.

Since it seems out of place to argue at this time the *merits* of the case, we now only state our insistence that the courts below erred in deciding each of the questions and matters stated adversely to your Petitioner; and that the Gifts and Partnership involved were each valid under the controlling Federal and State statutes and rules of

law; so that the refusal to allow a determination of the alleged income tax deficiencies in each of the tax years in question was error.

Only slight elaboration will here be added to the statement of "Questions" and "Reasons for Granting the Writ," as made in the Petiton, since we hope that these have been presented with sufficient clarity to avoid the necessity of burdening the Court with argument thereon.

This Brief, therefore, is devoted almost wholly to a summarized analysis of the *Opinions* below, in showing that the holdings on the *"Questions"* hereinbefore stated were controlled by erroneous rules of law, as indicated; and—*for reference* by this Court if desired—to a more detailed statement of the facts.

Jurisdiction

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. A., Sec. 347). The judgment of the Circuit Court of Appeals for the Fifth Circuit was entered on November 9, 1945 (R. 206-209). Petitioner filed her petition for rehearing on November 29, 1945 (R. 210); and the Circuit Court of Appeals entered its order and judgment denying such petition for rehearing on December 28, 1945 (R. 218).

Opinions of the Courts Below

Tax Court. The decision of the Tax Court and its Memorandum Findings of Fact and Opinion, pursuant to which the decision was entered, have not been reported; but the former appears in the Record at pages 84, 85, and the latter (relating to Petitioner) at pages 34-44, 46-52, 55-71, 76-78.

As to Gifts. The Tax Court in its opinion recognized that "a manual delivery of stock certificates is not always necessary to consummate a valid gift of the stock, and under certain circumstances transfer on the books of the corporation in itself has been regarded as a sufficient delivery." (Citing decisions to that effect.) But the Tax Court failed to apply those decisions, and held that it was not necessary to decide whether the "*manner of delivery*" was sufficient, because of its holding in the case that "the actions of the parties *subsequent* to the transfers (of stock) in question were such as to negative the existence of *donative intent* in each case" (All added emphasis in this Brief ours); that, to make a valid gift, there must be "the irrevocable transfer of the present legal title and of the dominion and control of the entire gift to the donee, so that the donor can exercise no further act of dominion or control over it; and a delivery by the donor to the donee of the subject of the gift or of the most effectual means of commanding the dominion of it" (Citing *Adolph Weil*, C. C. A. 5th Circuit, 82 F. 2d 561, 31 B. T. A. 899, 906); that "the subjective state of mind • • • must be found not only from their testimony of what they intended, but also from an examination of all the circumstances *surrounding* each transaction;" that "*surrounding* circumstances, including *subsequent acts* of the taxpayer, often establish intent more clearly than the words of the participants" (citing Tax Court decisions); and, as above stated, "we think the *actions* of the parties *subsequent* to the transfers in question were such as to negative the existence of *donative intent*" (Memo. Opin. 47, 48, 52). However, in dealing with the question of fraud penalties and tests therefor, the Court held: "In our opinion the evidence of fraud in the instant proceedings does not meet those tests. It is one thing to hold that the petitioners did not make *completed* gifts of the stock transferred to

their wives, but quite another to say that their failure to report the dividends thereon was motivated by fraud *and unlawful intent* (Citation). It is possible that they had the opinion that what they did was *legally sufficient* to relieve them of liability for tax. • • • We disagree with their contention that the transfers had that effect, but *cannot say that they were shams designed to evade tax*" (R. 77, 78).

Court of Appeals. As to *Gifts*—the Court of Appeals (151 F. 2d 806; Adv. Sheets; R. 206-209, 218), in affirming that decision, and in holding that "among the indispensable conditions of a valid gift is the intention (of the donor) to absolutely and irrevocably divest himself of title, dominion, and control of the subject of the gift," cited as the basis therefor decisions without pertinence to any questions relating to the alleged gifts except as to the *manner of delivery* necessary to make a valid gift of corporate stock; the decision cited thereon indicating, as the Tax Court also indicated by its language above quoted and citation of the *Weil* decision (82 F. 2d 561, 31 B. T. A. 899, 906), that a physical delivery of corporate stock certificates, besides a transfer on the books, was necessary. As to *Gifts*—the Appellate Court in its opinion made no express reference to the Federal income tax statutes, or special rules relating to their construction, or State rules, but ignored them, and treated the gift question, under general law, as one of gift or no gift depending "upon the *intent* of R. A. Sewell in making the gift," and held this "was a question of fact that the Tax Court has answered adversely to the contention of the Petitioner" (R. 208). The courts below dealt with the question of donative intent or dominion and control as one under general law, but failed to apply the correct rules of general law, or of local law, or of Federal law under the income tax statutes.

As to *Partnership* (in 1936 or 1937)—the *Tax Court* based its decision thereon primarily upon its preceding holding that the alleged stock *gifts* were invalid, and therefore the stock and its proceeds always belonged to R. A. Sewell, the husband; and Josephine M. Sewell, never having had anything to contribute, contributed nothing to the partnership capital, and never became a partner. The Tax Court noted, but failed to apply, the rule that "the fact that the capital contributions made by the wife or the children were acquired by *gift* from the husband or parent is not determinative against the existence of such a partnership"—since, as the Court held, "the Petitioner's position here * * * is not that the decedent made a *gift of a capital interest* in the hat business to his wife, but rather that she *purchased* such an interest with funds of her own. (Reference to this misconstruction of the Record as to her 'position' is made under 'Additional Facts' in this Brief and in the preceding petition.) That position we have already held untenable." The Tax Court further held that it need not consider "whether under different circumstances there would have been *gifts of a capital interest* to Mrs. Sewell, and by her in turn to the children." For the same reasons, it failed to consider what effect the written trust agreement between Mr. and Mrs. Sewell (even if not executed until the middle of 1937), and the limited partnership agreement between them individually and as trustees, both by undisputed evidence having been made by July 1, 1937, had upon the existence of a *limited* partnership (valid under Georgia law); and what effect the preceding oral agreement as to a *general* partnership and as to the trust interests given to their four minor children had upon such a partnership, in either 1936 or 1937. And the Court simply held that no sort of partnership ever existed; adverting to the fact that "the record does not indicate the extent to which Mrs. Sewell *participated in the*

management of the business," with a slight exception noted, and the fact that "she took no particular part in the *actual running of the business*" (R. 67-71).

The *Court of Appeals* (151 F. 2d 806, Adv. Sheets; R. 206, 209, 218) affirmed generally these holdings, ruling that the Tax Court's conclusion "on the invalidity of the family partnership is equally well founded *in law and fact. The funds that went into the establishment of the alleged partnership were the money and property of the husband,* under the decision of the Tax Court. All the evidence leads to the conclusion that (he) *was the sole owner* of the hat business during the tax years here under consideration * * * the decision of the Tax Court is supported by substantial evidence" (R. 208). The decision cited to support this holding (except the familiar ones laying down rules as to trusts, income or corpus questions in tax cases, in no wise pertinent to the instant questions) were partnership cases where the profits or earnings depended upon the *technical skill* or *personal services* of the husband in a business of such type, but not a mercantile or manufacturing business as in the present case. Both Courts failed to apply the local law of the State, recognizing the validity both of general and limited partnerships where the wife contributes only to capital, without actively participating in the management or control of the business.

Additional Facts

In the *Questions* stated in the preceding Petition, the uncontroverted facts required for each determination (as is necessary in nearly all questions of law) have been integrated as briefly as possible. But for *reference,* if a more detailed picture is desired as to any question, a summary is here added, with notations where the particular facts appear in the Record.

During the transactions involved, Sewell Manufacturing Company was a Georgia corporation, in which R. A. Sewell, his two brothers and others (including the secretary and treasurer) were stockholders; the former being chairman of its board of directors (R. 109, 133, 173, 185, 193, 194; Memo. Opin., R. 37). On January 2, 1934, R. A. Sewell, after having stated to his wife, Josephine M. Sewell, and to others, his intention to give her stock of the Company, "in order," as stated to one, "to provide for his wife and children," had stock certificates for 1,000 shares in the Company, standing in his name, marked "Canceled" and new certificates therefor issued in her name, sealed and signed by the Company's officers. These certificates were not physically delivered to her, but according to the practice of the Company and its stockholders (including holders outside of the Sewells), remained in the Company's stock certificate book, kept at all times in the vault at its offices, and there accessible to Josephine M. Sewell. On July 31, 1936, under similar facts, R. A. Sewell made to her a transfer of 300 additional shares. (R. 104, 105, 108, 109, 112, 113, 122, 123, 152, 175, 178, 186, 189, 195, 196; Documentary Evidence, W. P. Sewell case, Exhibits 1, 2—Certificates of Stock Nos. 8, 11-13, 38-41, 44, 45, 75; Doc. Ev. R. A. Sewell case, Exh. 13; Memo. Opin., R. 37, 38).

Josephine M. Sewell did not indorse any of the certificates at the time of their issuance to her, or earlier than in the following Fall or not until about the time of a first sale of stock by her on December 29, 1934; subsequent sales being made on June 1, September 21, and October 5, 1935; on October 31, 1936, and on October 31 and November 9, 1937 (R. 113, 117, 123, 155; Petrs. Doc. Ev., Exh. 13). On October 31 and December 18, 1936, she also executed written pledge contracts to secure loans to her, covering 317 of the shares that had been assigned to her in

the alleged gifts; these instruments (as to stock held in her name) being signed by Mrs. Sewell herself as pledgor and by the pledgees, and recorded in the public records; the validity of such instruments for their purported purpose not being questioned in this case, their reality being recognized by the Tax Court in its findings and opinion as to whether gains were taxable in 1936 or 1937 (R. 129-132; Memo. Opin. 57-62; Petrs. Doc. Ev., Exhs. 13, 22-26).

"In the handling of the financial affairs of (the) corporation" with its stockholders, its books were "practically made • • • a bank" by the president for their use; the Sewells and other stockholders having "a financial account on (its) books. The dividends were paid merely by crediting them on the books." Monies due to or by them were handled by debit and credit entries. Josephine M. Sewell and R. A. Sewell had such separate accounts. In 1934, dividends of $14,000 for that year on the stock in question were thus credited to her account. On December 29, 1934, proceeds from a sale of part of the stock involved were also thus credited to her account. Such 1934 monies remained to her credit (subject to her disposal as she desired, so far as shown by the Record), until a debit for payments of her income taxes in March 1935, and a transfer of the balance in her account to the account of R. A. Sewell on May 20, 1935. Later, other credits were entered in her account during June, September, and October 1935, and February, March, April, May, October, and December 1936; consisting partly of dividends on the stock involved, but mostly of proceeds from her sales and pledges of such stock (as above stated), and interest on the monies to her credit charged against the Company. These monies remained to her credit, not withdrawn by her, until their transfer to R. A. Sewell's account on October 21 and December 30, 1935, and October 31 and December 18, 1936. Other than by such transfers of proceeds from the

stock to his account on the Company's books, and his use of such funds in building and equipping a hat manufacturing business, known as Sewell Hat Manufacturing Company and Sewell Hats (involved in questions as to whether that business was a partnership)—there was nothing to indicate any retention or assertain by him of dominion or control over the alleged gifts of stock or its proceeds (R. 175, 117, 121, 122; Petrs. Doc. Ev., Exhs. 20, 21, 13, 18, 19; W. P. Sewell case, Exhs. 1, 2).

Early in 1935, R. A. Sewell made to the Government income tax authorities a sworn Gift Tax Return, reporting the 1,000-shares alleged gift (made on January 2, 1934), and in 1937 the 1936 alleged gift of 300 shares, and paid the Gift Taxes on both transactions. Josephine M. Sewell attached to each of those Returns her signed acknowledgment of the gift, certifying to the Government that "all the information given herein is correct" (Petrs. Doc. Ev., Exhs. 1, 3; Memo. Opin., R. 38, 39). She also made Individual Income Tax Returns to the Government, returning as her income the dividends and profits from sales and pledges of the stock in question during those tax years, and paid the taxes thereon. R. A. Sewell in his Individual Returns for those years made no such inclusion (Petrs. Doc. Ev., Exhs. 7-10).

As to *Partnership* of Sewell Hat Manufacturing Company or Sewell Hats—Mrs. Sewell's testimony was that she had "loaned" to her husband the monies transferred to his account on the corporate books of Sewell Manufacturing Company, to be used in the building and equipment of the plant (under the former trade name). The testimony of the Government's revenue agent was that, although she denied to him having made any "loan" to her husband, she informed this agent as to the alleged gifts and the dividends, and stated to him that "she knew every time a dividend was credited to her account her in-

terest in the business was increasing, and that she left them in the business so that the Company could avoid making bank loans," and that her husband "had her permission in his capacity as directing head of the Company (chairman of its directors) to use them for the Company's benefit" (R. 152, 153, 155, 156, 160). The funds from the wife's account thus used in the creation or operation of the hat business amounted to a total of $222,255.54, while Sewell's contribution to the capital from other funds amounted to $138,945.07. The Tax Court found similar proportionate investments (Memo. Opin. 62; Petrs. Doc. Ev., Exhs. 18, 19; R. 121, 122).

Mr. and Mrs. Sewell orally agreed that, by reason of her contribution of monies used by him in building and equipping the hat plant, a partnership would exist between them, from the beginning of the 1936 business, which started on February 27, 1936; after a 1935 sole proprietorship by Sewell, the taking over and operation of the business by W. P. Sewell in the latter part of that year, as "a brotherly act", during an illness of R. A. Sewell, and the deed of the properties back to the latter after his recovery. Although there were no entries on the books of Sewell Hat Manufacturing Company until the close of business, December 31, 1936, when the wife's alleged interest was entered, R. A. Sewell during 1936 informed several persons as to the existence of a partnership between him and his wife. A witness for the Government, familiar with the financial transactions of the parties, testified that it was his "understanding there was a verbal partnership" between husband and wife, which was carried forward later into a limited partnership. This was under a written trust agreement and a limited partnership agreement, the former executed as a formal instrument about the middle of 1937 (although it bore date of June 1, 1936), and the latter on July 1, 1937. Under those instruments, it

was agreed that the husband and wife had equal interests; and their four minor children (at first having a 20 percent interest) a 33⅓ percent interest; the husband and wife being made trustees as to such interests; and the evidence being that the husband and wife had previously orally agreed as to those interests. Under the limited partnership instrument, Sewell was the general partner, and the wife and children limited partners; the formalities of the Georgia statutes as to such partnerships being complied with.

The written trust agreement recited that Mrs. Sewell had "*purchased* and paid for" her undivided interest in the hat manufacturing business; to which reference was made by the Tax Court in its Findings and Opinion (as heretofore stated). The Record nowhere indicates that she as Petitioner (executrix of the decedent), in her contentions as to a partnership in both 1936 and 1937, has based her position upon a "purchase" of an interest, any more than upon a gift, or upon an implied trust (created by Georgia law in favor of a wife whose husband uses her monies either "with or without the wife's consent"), or upon any particular theory other than her contribution to the capital, the husband's use of her monies, the oral and written agreement as to a partnership, and the operation of the business as such.

In financial statements to obtain credit filed by Sewell with two banks as of May 31, 1936, he stated that he was the owner of the business. There was nothing else to indicate his proprietorship during 1936 or 1937 except his management of the business without the active participation of the wife. In March, 1937, he filed with the Government tax authorities a Partnership Return as to Sewell Hat Manufacturing Company for 1936, showing that it was a partnership composed of Mrs. Sewell and himself, owning a 40 percent interest each, and their four chil-

dren owning 5 percent each, with the profits of the business divided accordingly. He filed in February 1938 a like return for 1937, showing (according to the trust and limited partnership agreements) a limited partnership composed as stated, with a 33⅓ percent interest in each parent, and 8⅓ percent in each child. Gift tax returns as to the parents' gifts to the children of their interests were also filed with the Government. In their separate Individual Income Tax Returns, Mr. and Mrs. Sewell showed profits accruing to them from the business as a partnership, and not as a sole proprietorship owned and operated by him. In 1938, Reconstruction Finance Company lent $75,000 to the business as a partnership, and Mr. and Mrs. Sewell, signing individually and as trustees, executed the security deed as a partnership (R. 151-154, 135-137, 140, 128, 124, 125, 141, 143, 165, 167, 145-147, 148, 149, 120, 122; Petrs. Doc. Ev., Exhs. 5, 10-12, 14-19, 31, 32; Respondent's Exhs. A, B; Memo. Opin. 63-71).

Assignments of Error

Under Rule 38 (par. 2) of this Court, we have embodied with the "Questions Presented" in the Petition the errors especially to be considered, to which we respectfully refer, without repetition, as part of this Brief. We respectfully insist that the Court of Appeals and the Tax Court erred in decided adversely to Petitioner on each of the grounds set forth in her Petition for Review (R. 88-100).

Argument

1. The decisions of the courts below were manifestly based, as to both Gifts and Partnership, on clear-cut errors of law, in applying to uncontroverted facts erroneous legal standards, criteria, and rules, and in failing to apply the true and correct legal principles.

2. The decision, as to donative intent in gifts and their nullification, long after completion, by the donee's mere use of proceeds from the gifts, and the decision that the transfers of stock on the corporate books did not complete the gifts (taken with the uncontroverted acts of the parties), and in failing to apply to the gifts in question the rules of local law making such a constructive or symbolic delivery sufficient, were each in conflict with the decisions of the Circuit Courts of Appeal and of the State of the transactions, as stated in the Petition, as well as contrary to previous decisions of the courts below themselves, and contrary to general law.

3. The decision, as to partnership, that there had been no valid gifts by husband to wife, that she had "purchased" no interest in such business and contributed nothing to the capital (erroneous as a matter of law for the reasons heretofore stated), and the decision making the husband's management of the business and the wife's lack of participation a controlling factor on the question of partnership, were each in conflict with the decisions of this Court, the Circuit Courts of Appeal, and Georgia, as stated in the Petition.

4. The particular questions, never decided by this Court, are vitally important to all who are concerned in a proper construction and administration of the Federal Income Tax Statutes.

1

Errors of Law. The preceding analysis of "Opinions of the Courts Below," with the "Questions" and "Reasons" stated in the Petition, we believe will suffice, without additional argument, to show clearly the reviewability of this case, if it appeals to the discretion of this Court as proper for review under Rule 38 (5, b).

2

Conflicts in Decisions as to Gifts. We earnestly appeal to the discretion of the Court for the grant of a writ of certiorari, because of the conflict between the decision of the Circuit Court of Appeals and the decisions of the Circuit Courts of Appeals for other Circuits, and Georgia decisions, as stated in the Petition, under the holdings of the courts below that essential donative intent in gifts is nullified by the donee's mere use of the proceeds, after the completion of all that was necessary to make a valid gift, and too long thereafter to have any significance, pertinence, or relevancy; and under the holdings of the courts below, failing to apply to the question as to valid gifts the rules of local law making a constructive or symbolic delivery sufficient, and failing to hold, as a matter of law, that the transfers of corporate stock on the books of the company, with other acts of the parties—all being without fraud or sham—made complete and valid gifts for Federal income tax purposes.

Such decision is also contrary to that in *Tower* v. *Commissioner* (6th Circuit Court of Appeals), 148 F. (2d) 388, 390 (in which a writ of certiorari has been granted), where a gift and partnership between spouses were sustained, although the facts were not as strong as here, the husband attaching a condition to the gift, and the question of mere "sham" was involved, instead of the present finding that there was no fraud of "shams designed to evade tax." (R. 78.) The appellate court decision and the holdings of the Tax Court also conflict with their own earlier decisions: in *Kell* v. *Commissioner* (5 C. C. A.), 88 F. (2d) 453, that, after completion of the gift and a partnership interest, the donor's use or handling of monies was "without significance to change the legal import and effect of his verbal and written direction;" in Tax Court cases cited with Circuit

Courts of Appeals decisions, but not applied, in the Memorandum Opinion (R. 52); and in *Southern Industrial Institute* v. *Marsh* (5 C. C. A.), 15 F. (2d) 347, nullifying a stock gift because of a condition imposed thereon, but holding that "the validity of the gift depends upon the laws of Georgia." The decision is also contrary to general law; citations being here out of place.

3

Conflicts in Decisions as to Partnership. Such conflicts with particular decisions have been fully indicated in paragraphs 3, 4, and 5 (b, c), under "Reasons for Granting the Writ," in the Petition. The decisions of the courts below, as to capital contribution by a wife, the husband's active management, and the wife's lack of active participation in the business, also conflict with many decisions by the Tax Court itself, sustaining such a partnership, unless the business is essentially one of the personal-service type where capital is not a factor of any moment in producing the income, and including: M. W. Smith, Jr., 3 T. C. 894; Robert P. Scherer, 3 T. C. 776; Davis B. Thornton, 5 T. C. 13; Felix Zukaitis, 3 T. C. 814; Estate of J. W. Holtiwanger, T. C. Memo. Op., Dkt. 4469 (Jan. 18, 1945); Julius Caesar Haley, T. C. Memo. Op., Dkt. 5568 (Jan. 23, 1945) (as to minors becoming partners by gift where permitted by State law); Glensder Textile Co., 46 B. T. A. 176 (recognizing limited partnerships where good under State law).

4

Important Federal Questions undecided by this Court. We believe that no elaboration of paragraph 6 of the Petition, under "Reasons for Granting the Writ", is necessary to demonstrate the vast importance of the questions, which remain undetermined by this Court, as to gifts and

partnerships in the light of the Federal income tax statutes, and as to whether and to what extent local law controls or is to be considered in such transactions, if there is no fraud, sham, or fiction, and the formalities (valid under local law, as under general law) are realities.

In conclusion, however—besides the importance of settling the conflicts with decisions of other Circuit Courts of Appeals and with local decisions—it seems to us that the views of tax writers on the unsettled situation with regard to these matters are pertinent. One scholarly authority has said: "One may assume from many dissents that the Tax Court has recently been having an internal struggle with the husband-wife partnership problem. Typical cases present the disparity of opinion within the court." Paul, Partnerships in Tax Avoidance, Vol. 13, No. 2, George Washington Law Review, p. 125. Another writer has expressed a like view: "A regrettable and unsettling condition has been created in which the majority court hands down several decisions rejecting partnerships between husbands and wives, and, two days later, *upon substantially the same facts,* sustains such partnerships. Each case carries with it dissenting opinions of as many as five members of the court. In two cases, one judge writes the majority opinions and the dissenting opinions in the cases immediately succeeding. This condition is not conducive to fostering the qualities of stability and confidence which courts must possess if their opinions are to be respected." Polisher, Family Partnerships, Taxes, Vol. 22, No. 7, p. 300.

Without adopting such views as our own, and with all deference to the United States Circuit Court of Appeals for the Fifth Circuit and to the Tax Court, we most earnestly believe that the legal rules and standards with respect both to gifts and to partnerships, under Federal income tax statutes and previous rules and under local laws, should

be settled and clarified by this Court, particularly as to the questions raised in this petition; that the correct principles should be established as they have been in cases involving trusts and corporations; and that rules thus laid down would be of incalculable value to all interested in the proper construction and administration of such laws. For these and other reasons stated in the Petition and this Brief, we sincerely believe that this is an eminently proper case for the grant of a writ of certiorari.

Respectfully submitted,

OLIVER C. HANCOCK,
CLIFFORD R. WHEELESS,
Counsel for Petitioner.

APPENDIX

Federal Statutes

From Revenue Act of 1934, c. 277, 48 Stat. 680; identical provisions with corresponding numbers in Revenue Act of 1936, c. 690, 49 Stat. 1648:

"Sec. 11. *Normal Tax on Individuals.*—There shall be levied, collected, and paid, for each taxable year upon the net income of every individual, a normal tax * * *."

"Sec. 12. *Rate of Surtax on Individuals.*—(b) There shall be levied, collected, and paid for each taxable year upon the surtax net income of every individual, the surtax shown in the following table: * * *."

"Sec. 22. *Gross Income.*—(a) *General Definition.*—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever * * *."

"Sec. 181. *Partnership Not Taxable.*—Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity."

"Sec. 182. *Tax of Partners.*—There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year."

From the above Revenue Act of 1934, Section 801 (a) (3), and Revenue Act of 1936, Section 1001 (a) (3) (Internal Revenue Code, Section 3797 (a)(2)):

"The term 'partnership' includes * * * a group, pool, joint venture, or other unincorporated organiza-

tion, through or by means of which any business, financial operation or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term 'partner' includes a member in such a * * * group, pool, joint venture, or organization."

GEORGIA STATUTES FROM CODE OF 1933:

"48-101. *Essentials of Gift.*—To constitute a valid gift, there shall be the intention to give by the donor, acceptance by the donee, and delivery of the article given or some act accepted by the law in lieu thereof."

"48-102. *Acceptance of Gift.*—If the donation shall be of substantial benefit, the law will presume the acceptance, unless the contrary shall be shown * * *."

"48-103. *Delivery.*—Actual manual delivery shall not be essential to the validity of the gift. Any act which shall indicate a renunciation of dominion by the donor, and the transfer of dominion to the donee, shall be a constructive delivery."

"53-404. * * * The husband * * * may at any time during the coverture, either through trustees or directly to his wife, convey any property to which he has title, subject to the rights of prior purchasers or creditors without notice."

"75-101. *Manner of Creating Partnership.*—A partnership may be created either by written or parol contract, or it may arise from a joint ownership, use, and enjoyment of the profits of undivided property, real or personal."

"75-206. *Interest of Each Partner; Liability for Losses.*—Unless otherwise provided in the agreement, partners shall be equally interested in all the stock or property brought into the business, it matters not by which; partners shall be equally entitled to share the profits and equally bound to pay the losses."

(Limited Partnerships) "75-401. *Formation: Nature of Business.*—A limited partnership, for the trans-

action of any mercantile, commercial, mechanical, manufacturing, mining, or agricultural business within this State, may be formed by two or more persons, upon the terms, with the rights and powers, and subject to the conditions and liabilities herein prescribed; but the provisions of this Chapter shall not be construed to authorize any such partnership for the purposes of banking or insurance."

"75-402. *How Constituted: General and Special Partners.*—Limited partnerships may consist of one or more persons, who shall be called general partners, and who shall be jointly and severally responsible as general partners, and of one or more persons who shall contribute in actual cash a specific sum as capital to the common stock, who shall be called special partners, and who shall not be liable for debts of the partnership beyond the fund so contributed by him or them to the capital, except as hereinafter provided."

"75-403. *Authority of General Partners.*—The general partners only shall be authorized to transact business, and sign for the partnership, and to bind the same."

Sections 75-404 to 75-406 inclusive and 75-409 provide as to the nature of the certificate or agreement to be signed by the persons forming a limited partnership, acknowledgment thereon, filing for record, recording, and publication of terms of partnership for six weeks before the registry.

"75-417. *Liability of General Partners.*—The general partners shall be liable to each other, and to the special partners, for their management of the business of the firm, both in law and equity, as other partners are liable."

"108-114. *For Whom Trusts May Be Created.*—Trust estates may be created for the benefit of any minor * * *."

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CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 889

ESTATE OF R. A. SEWELL, JOSEPHINE M. SEWELL, EXECUTRIX,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

ADDENDUM TO BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

Neither the *Tower* nor the *Lusthaus* decision determined the essential Questions or obviated the Reasons for Granting the Writ, as stated in the instant petition. (Cases cited in preceding Motion.)

(A) Gifts

Neither case involved questions as to the taxability of income from a corporate-stock alleged gift, or passed upon the validity of such a gift—effected (as in this case) by a constructive delivery, followed and completed (if further acts were necessary) by the donee's formal acceptance of the gift, indicated to the Government by her signed writing attached to the donor's gift tax return, and by her own pledges and sales of the subject-matter of the gift.

While the *Tower* case involved alleged invalidity, as incomplete, of the alleged gift of stock by husband to wife, because of the express *condition* attached that she place the corporate assets represented thereby in a proposed partnership—effected only 3 days after the transfer and practically contemporaneously therewith—the decision by the Court majority did "not find it necessary to decide this issue." (Slip Opinion, p. 7.) Nor did the *Lusthaus* case pass upon the effect of the money gift, from husband to wife, "which he had given her *conditioned* upon her turning it back to him" (Slip Opinion, p. 3. All emphasis herein ours); such alleged gift being part of the formation of the alleged partnership.

In both cases, all questions relating to the alleged gift were merely incidental to the one issue of Partnership or No Partnership, and the taxability of profits from such business.

In the instant case, there are two basic issues—Gift, and *more than 2 years thereafter,* Partnership. Some of the most vital questions relate to the validity (for income tax purposes) of such a Gift, and the taxability thereafter, to the husband or the wife, of dividends, interest, and profits accruing therefrom. Neither of the two decisions stated solved such questions, or resolved the conflicts, stated in the petition, between the present Court of Appeals' decision and those of other Courts of Appeals and other decisions: as to a Gift of the character involved, particularly where the Tax Court has found that no "shams" existed; where the uncontroverted evidence showed that the donor never at any time exercised any control over the subject-matter of the Gift (the stock); and where there was nothing whatever to support the Tax Court's finding and conclusion as to the invalidity of the Gift because of the absence of donative intent, unless it be the use by the hus-

band—more than 16 months after the transfer and subsequently—not of the stock, but of dividends, interest, and proceeds therefrom after the wife's own sales and pledges of the stock. Without arguing the merits, save only so far as is necessary for this petition—we insist that such a theory is manifestly erroneous and in conflict with the decisions stated in the petition, without precedent in Federal income tax, or general, law, and renders the situation one which the *Tower* opinion recognizes as a proper basis for appellate review, where "the Tax Court erroneously disregarded or improperly applied certain legal principles" (Slip Opinion, p. 5).

(B) Partnership

Both the *Tower* and the *Lusthaus* cases, where Gifts were made only to form family partnerships, and contemporaneously therewith, involved the question of sham, artifice, or fiction—the reality or unreality of the forms employed in creating an alleged, but not actually intended, partnership for the sole purpose of avoiding or reducing Federal surtaxes. This is manifest in both decisions. The Court so indicated in the *Tower* case by its use of these words and phrases: "sham," "no real partnership," "really and truly intended," "really exists," "real or pretended," "mere paper allocation of income," "no genuine union" (Slip Opinion, pp. 2, 5, 7-9); and in the *Lusthaus* case, by "supposed husband-wife partnership," "merely superficial," "outer garment of respectability," "not a genuine partner" (Slip Opinion, pp. 1-3).

In the instant case, the Tax Court found that there was no fraud, fraudulent pretense, or shams. As to *Partnership,* its decision (as affirmed by the Circuit Court of Appeals), while mentioning the wife's non-participation "in the management" or "actual running of the business," was not based on those factors, any more than it was based on

the principle of sham or fiction, or on a husband's continued control or economic ownership, such as invalidated the *Tower* and *Lusthaus* partnerships. The Tax Court (as it had previously recognized the validity of family partnerships based upon *gifts*, and had recognized the sufficiency of a capital contribution without management or active participation in a non-personal-service or non-technical-expert partnership) here recognized, by mention and citations, the same principle as to Gifts of Partnership Interests. But the Court failed to apply such principles, and held that it need not consider this or other factors as to the effect of the oral or written partnership agreements. This was because it misconstrued and misapplied what it considered the controlling rules of law, in holding that: "The Petitioner's position here * * * is not that the decedent made a gift of a capital interest in the hat business to his wife, but rather that she purchased such an interest with funds of her own. That position we have already held untenable" (Record, 68-71; Petition for Certiorari with Brief, pp. 29, 30; Questions 6-8; pp. 9-13).

In thus basing its ruling as to no Partnership on the alleged absence of any "*purchase*" by the wife of an interest therein, the Tax Court planted it on the previous erroneous ruling that there was no completed, valid *Gift*. That Court and the Court of Appeals thus ignored the undisputed facts: that such Gift of stock, in an independent, still-continuing corporate business, occurred more than 2 years before the creation of the alleged Partnership (the former in January, 1934, latter in February, 1936); that, so far as in any wise indicated, the formation of such a Partnership was not remotely in mind at the time of the previous Gift; that, not until 16 months after the Gift, did the husband (who was a stockholder and chairman of directors, with others, in the corporation) first use funds de-

rived from the stock Gift, in starting to build the plant of the hat business, which became part of the assets of the subsequent alleged Partnership; that, whether or not the wife's contribution to capital under the oral and written partnership agreements—by way of satisfaction or repayment to the wife for her funds used and to be used in the business—rested upon a *loan* to him (which the Commissioner contested), or rested upon his mere use of such monies either with or without her consent, the wife already had, under the law of Georgia (as shown in the Petition), an implied trust enforceable against the hat-business assets (an actual beneficial ownership given to her by law in such business), which afforded an ample and valid basis for her capital contribution under the partnership agreement, whether by "purchase" or otherwise.

Neither the *Tower* nor the *Lusthaus* case decided any such questions. If, here, the husband and wife in fact made no actual gift, no genuine partnership, under their continual sworn returns, written receipt for the stock gift, and acts through the years, they necessarily perpetrated upon both the Commissioner and the Reconstruction Finance Company (which took their mortgage as a partnership for a large amount), not only a barefaced sham, but a gigantic fraud. Yet the Tax Court found no fraud or shams.

Stripping its opinion of other facts in the companion cases, tried at the same time, but inapplicable to this Petitioner (probably confusing the Tax Court), the sole tangible basis for its rulings seems to have been the erroneous conception that mere use by a donor of proceeds from a Gift, lent or used with or without the donee's consent, more than 16 months after the Gift, without any previous attached condition, agreement, or understanding as to such use, is sufficient to negative donative intent, so as to nullify the Gift; and the conception that a mere relationship of husband

and wife, coupled with a desire to avoid and reduce Federal surtaxes (though there was no evidence as to any such expressed motive in this case), will defeat both a Gift and a Partnership for income tax purposes. Such latter conception is unsupported by either the majority or minority opinions in the *Tower* and *Lusthaus* cases.

Because of these errors of law, as to the novel and important questions involved, and the need for settling the conflicts stated in our petition, and because we believe that this Court should now differentiate between actual, bona fide gifts and partnerships (not involving technical trust agreements) where the dealings are realities—even though in a family group—and mere shams of fictions, and should now determine whether or not local law as to Gifts and Partnerships, or either, should be applied in such no-fraud, no-sham cases, we respectfully submit that this case is a meritorious one for the exercise of the Court's discretion in granting a certiorari.

Respectfully submitted,

OLIVER C. HANCOCK,
CLIFFORD R. WHEELESS,
Counsel for Petitioner.

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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 889

ESTATE OF R. A. SEWELL, JOSEPHINE M. SEWELL, EXECUTRIX, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 34–78) is not officially reported. The opinion of the Circuit Court of Appeals (R. 206–209) is reported at 151 F. 2d 806.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 9, 1945 (R. 209) and a petition for rehearing (R. 210–217) filed on November 29, 1945, was denied on December 28, 1945 (R. 218). The petition for a writ of certiorari was filed on February 26, 1946. The

jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. The Tax Court determined that the taxpayer did not intend to make a completed gift to his wife of certain income producing property and that he was not thereby relieved from liability for the tax imposed on the income by Sections 11 and 22 (a) of the Revenue Acts of 1934 and 1936.

Did the Circuit Court of Appeals err in deciding that the Tax Court's conclusions were supported by the evidence?

2. The Tax Court determined that a partnership did not, for tax purposes, exist between taxpayer and his wife and children, and that all the profits from the purported partnership were taxable to the taxpayer.

Did the Circuit Court of Appeals err in holding that the decision of the Tax Court was supported by the evidence?

STATUTES INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 11. NORMAL TAX ON INDIVIDUALS.
>
> There shall be levied, collected, and paid for each taxable year upon the net income of every individual a * * * tax * * *.
>
> * * * * *

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from * * * professions, vocations, trades, businesses, commerce, * * * or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, * * * dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

The corresponding provisions of the Revenue Act of 1936, c. 690, 49 Stat. 1648, are identical.

STATEMENT

This case involves the income tax liability of R. A. Sewell (hereinafter referred to as the taxpayer) for the taxable years 1934–1937, inclusive. This case arises from a consolidated proceeding before the Tax Court from which a separate petition for review was taken to the Circuit Court of Appeals for the Fifth Circuit.[1] The facts found by the Tax Court relating to the present proceeding may be summarized as follows:

[1] A separate petition to review the Tax Court's determinations respecting the liability of the taxpayer's two brothers resulted in an affirmance. *Sewell* v. *Commissioner*, 151 F. 2d 765 (C. C. A. 5th), certiorari denied, February 25, 1946, No. 754, this Term. That case presented issues similar to the first issue here involved.

The taxpayer was one of the principal stockholders of the Sewell Manufacturing Company. In 1934, at the taxpayer's direction, the accountant for the company prepared five stock certificates for a total of 1,000 shares of stock of the company in the name of the taxpayer's wife, Josephine M. Sewell; certificates for a like amount of shares which were standing in the taxpayer's name were cancelled. The taxpayer's wife was not present at the time of the issuance of the certificates and has never had possession of them. The certificates were at all times attached to their stubs in the company's stock book. The taxpayer advised his wife that he had made a gift of the stock. (R. 37–38.) In a similar manner in 1936, 300 shares were issued to the taxpayer's wife, and two certificates for the same number of shares which were then in the taxpayer's name were cancelled. (R. 38.) Gift taxes were paid on these purported gifts. (R. 38–39.)

The taxpayer's wife took no part in the management or in the business of the company; she did not have notice of or attend any stockholders' meetings, but did come to the office occasionally and had access to the company's vault which was left open during business hours. At the time of, or subsequent to the issuance of the certificates, she endorsed them in blank, some of the endorsements not having been made until the times when her shares were sold. (R. 39.)

During the years 1934 through 1936, dividends in the total amount of $47,006.60 were credited on the books of the company to the account of the taxpayer's wife. There was also credited to her account $175,768.72 which resulted from the proceeds of sales or of loans of the stock standing in her name. (R. 40–41.) During the taxable years there was transferred on the books of the company to the taxpayer's account from his wife's account the amount of $222,255.44. (R. 41–42.) The only other debit to the taxpayer's wife's account was for certain taxes paid for her. (R. 42.) These transfers were made by the company's bookkeeper who in some instances did so at the direction of the taxpayer and in others without any specific authorization. The taxpayer's wife knew that the taxpayer made some use of the dividends standing to her credit and agreed that he could do so at any time he needed money. (R. 43.) The taxpayer did not execute any promissory notes for the amount so transferred and he used the money, together with other funds, for the organization of a hat manufacturing business and for the construction and building of its plant. (R. 44.) In filing credit statements with certain banks to show the financial condition of this company, the taxpayer did not disclose that his wife had any financial interest therein, or that he was indebted to her. (R. 46.)

In transferring the stock the taxpayer did not intend to vest in his wife dominion and control over the shares, but intended to and did retain that control and dominion in himself. The taxpayer's wife knew that such an intention existed and impliedly agreed that the taxpayer should retain control of the stock that was issued in her name. (R. 46.) The Tax Court specifically found that (R. 46) "Completed gifts of the stock certificates so transferred were not made." As a result, the Tax Court concluded that the dividends on the stock were taxable to the taxpayer. (R. 47–52.)

During the years 1934 through 1936, gains were realized from the sale or exchange of certain of the stock which was standing in the name of the taxpayer's wife. (R. 57–59.) Pursuant to its conclusion that completed gifts of the stock had not been made, the Tax Court determined that such gains were taxable to the taxpayer. (R. 59–62.) The Circuit Court of Appeals affirmed on the ground that the Tax Court's conclusion was supported by the evidence. (R. 208–209.)

By the close of the year 1935, the taxpayer had invested $107,803.64 in a business known as the Sewell Hat Manufacturing Company, this amount having been transferred from his wife's account in the Sewell Manufacturing Company; he also invested an additional amount of $54,220.41. By the close of 1936, he had also invested $114,451.80 transferred from his wife's account during that

year and the additional amount of $84,726.66. (R. 62.)

In the fall of 1935, the taxpayer became seriously ill and his brother purchased the hat business, agreeing to reconvey it to the taxpayer at the same price whenever the taxpayer should desire. In the early part of 1936, the taxpayer requested and obtained a reconveyance of the business. An operating loss of $18,000 was sustained by the company in 1935 and the entire amount of the loss was claimed as a deduction by the taxpayer in his individual tax return for 1935. (R. 62–63.)

Although, in 1936, the taxpayer told his business associates that the hat business was being operated as a partnership, he represented himself as the sole owner in certain financial statements. The capital account in the company's ledger was opened on August 31, 1935, under the caption "Investment—Capital—R. A. Sewell". (R. 63.) In March, 1937, on instructions from the taxpayer, the bookkeeper added the words "and family" to the caption. At about the same time, and also upon the taxpayer's instructions, the bookkeeper inserted a sheet in the ledger showing a credit balance in the capital account as of December 31, 1936 (R. 63):

R. A. Sewell	$159,025.27
Josephine M. Sewell	159,025.27
R. A. Sewell, Jr	15,818.39
Joseph Sewell	15,417.24
Hugo Sewell	15,435.26
Helen Virginia Sewell	15,377.23

These figures were given to the bookkeeper by the accountant who was retained to examine the books for the preparation of a 1936 income tax return. On March 19, 1937, the accountant prepared a gift tax return for the taxpayer's wife on which she reported gifts on January 1, 1936, of separate $15,000 interests in the company to each of her four children. (R. 63–64.) A partnership return for the company prepared by the same accountant and executed on March 19, 1937, reported net income of $10,311.05, of which 40% was distributable to the taxpayer, 40% to his wife, and 5% each to the four children. The taxpayer's wife filed a tax return for 1936, which was prepared by the same accountant, but did not report any amount as her distributive share of the profits of the purported partnership. (R. 64.)

At about the time that these income and gift tax returns were under preparation, the accountant instructed one of his employees to prepare a trust agreement covering gifts from the taxpayer's wife to her four children. The trust instrument was completed on May 27, 1937 but bore the date of June 1, 1936. The instrument named the taxpayer and his wife as trustees and provided, in part, as follows (R. 64–65):

> Whereas, the party of the first part has this day purchased and paid for a three-fifths (3/5) undivided interest in a certain business, known as the Sewell Hat

Manufacturing Company, located at Red Oak, Fulton County, Georgia, and whereas the undersigned desires to convey in trust for each of her following minor children, to-wit: Robert A. Sewell, Jr., Joseph Sewell, Hugo Sewell and Helen Sewell, an undivided one-twentieth (1/20) interest in and to all of the assets of said business, and all profits therein accruing from and after this date, upon the terms, conditions and powers hereinafter set forth, and

Whereas, the undersigned desires that her husband, Robert A. Sewell, who is the owner of two-fifths (2/5) undivided interest in the business, continue the active management and control of said business, both for himself and for the benefit of said minor children, and for the benefit of the party of the first part,

Now Therefore, the party of the first part, in consideration of love and affection, does hereby transfer and convey unto herself and Robert A. Sewell, as Trustees for said named minor children, a one-fifth (1/5) interest, i. e., a one-twentieth (1/20) interest for each minor child, in and to said partnership, upon the following terms, conditions and powers, hereinafter set forth, that is to say:

1. The party of the first part does constitute, select, and appoint herself and husband, Robert A. Sewell, as Trustee for each of said described children during their minority, the said Trustees to hold legal title to said respective partnership

> interests and assets, for the use and benefit of said minor children, and the said business shall continue from and after this date as a partnership consisting of the party of the first part owning an undivided two-fifths (2/5) interest, her said husband, Robert A. Sewell, owning an undivided two-fifths (2/5) interest, and the aforesaid Trustees holding the legal title for each of said minor children, to an undivided one-twentieth (1/20) interest for the use and benefit of said children.

The taxpayer's wife subsequently signed the instrument. It was later lost and has never been recovered. On October 16, 1940, she executed a carbon copy of the original. (R. 66.)

During the time that the trust agreement was under preparation, the employee who drafted it was also engaged in the preparation of a limited partnership agreement between R. A. Sewell, individually, as general partner, and Josephine M. Sewell, individually, and R. A. Sewell and Josephine M. Sewell, as trustees for their four children, as limited partners. The final draft was completed about the same time as the trust agreement and was executed under the date of July 1, 1937. It provided that the taxpayer and his wife should each contribute to the capital of the limited partnership their separate undivided two-fifths interest in the Sewell Hat Maufacturing Company, and that, as trustees for their children, they should contribute four undivided one-twentieth

interests; that profits and losses should be divided in proportion to the capital contributions; that the taxpayer should have active charge of the conduct of the business, and be paid a salary not to exceed 40% of the net income of the business; and that in the event of his death, the partnership should terminate. (R. 66.) There had been no written partnership agreement affecting the hat business prior to the execution of the trust agreement and the limited partnership agreement in 1937. (R. 66.)

Under date of September 30, 1937, the capital investment accounts of the taxpayer and his wife were debited $20,000 each, and credits of $10,000 each were entered in the accounts of each of the four children. At that time, it was agreed that the distributive share of profits of each child should be 8⅓ percent. (R. 66.) A partnership return for the Sewell Hat Manufacturing Company for 1937 reported net income of $42,889.95, before payment of salaries of $8,400 to the taxpayer and $3,000 to his wife, leaving a balance of $31,489.95, distributable as follows (R. 67):

R. A. Sewell	$10,496.55
Jos. M. Sewell	10,496.55
R. A. Sewell, Jr.	2,624.22
Joseph Sewell	2,624.21
Hugo Sewell	2,624.21
Helen V. Sewell	2,624.21

The taxpayer's wife reported the amount of $13,496.55 as income from the hat business on her individual return for 1937. The amounts reported as her distributive share of the profits

and that of the four children, less withdrawals, were transferred in each of the taxable years and in subsequent years to the credit of their respective capital accounts. In 1937 withdrawals in the amount of $18,763.46 were charged to the taxpayer's wife, and of $47.50 to each of the four children. (R. 67.)

The taxpayer died on January 16, 1940. Thereafter the hat business was operated by his widow and the children. In 1942 it was incorporated and has been operated as a corporation since that time. (R. 67.)

The Commissioner determined that taxable income from the hat business was $11,670.43 in 1936 and $43,323.93 in 1937, and that the entire income for each year was taxable to the taxpayer. (R. 67.)

The Circuit Court of Appeals (R. 208–209) affirmed the conclusion of the Tax Court (R. 67–71) that the taxpayer was the sole owner of the business during the taxable years and the income therefrom was taxable to him.

ARGUMENT

1. Whether the taxpayer intended to make a completed gift of the stock in the Sewell Manufacturing Company to his wife, and whether he relinquished dominion and control over the shares or retained substantial ownership with respect to this property, were questions of fact for the determination of the Tax Court. *Commissioner*

v. *Court Holding Co.*, 324 U. S. 331; *Helvering* v. *Clifford*, 309 U. S. 331; *Dobson* v. *Commissioner*, 320 U. S. 489, 494, rehearing denied, 321 U. S. 231. The Circuit Court of Appeals, quite properly, reviewed only the evidence to determine whether it supported the Tax Court's conclusion. In view of the facts set forth in the statement, *supra*, there was more than sufficient evidence to sustain a finding that the taxpayer never intended to make a gift of the stock to his wife.

2. The decisions of this Court in *Commissioner* v. *Tower* and *Lusthaus* v. *Commissioner*, Nos. 317 and 263, this Term, decided February 25, 1946, demonstrate, beyond any question, that the courts below decided the family partnership issue correctly. There was ample evidence from which the Tax Court could conclude that all funds invested in the hat business always belonged to the taxpayer, that his wife did not purchase any interest in the business in 1936, that the 1937 trust agreement, under which she declared herself to be trustee for their children, was without foundation when it recited that she had purchased an interest in the hat business, and that the 1937 limited partnership agreement between the taxpayer, his wife, and their children was also not of probative value in its statement that she had an interest in the hat business. (R. 69–70.)

There was no contention before the Tax Court that the taxpayer had given his wife an interest

in the partnership either in 1936 or in 1937. Moreover, there was no documentary evidence of such a transfer and the Tax Court was justified in finding that not even a formal gift to the wife had been made. But even if there had been such a gift, this additional fact would not have been sufficient to alter the decision reached. *Commissioner* v. *Tower, supra* and *Lusthaus* v. *Commissioner, supra.*

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully.

J. HOWARD MCGRATH,
Solicitor General.

SEWALL KEY,
Acting Assistant Attorney General.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 889

ESTATE OF R. A. SEWELL, JOSEPHINE M. SEWELL, EXECUTRIX,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S REPLY BRIEF

OLIVER C. HANCOCK,
CLIFFORD R. WHEELESS,
Counsel for Petitioner.

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PETITIONER'S REPLY BRIEF

To the Honorable the Chief Justices and the Associate Justices of the Supreme Court of the United States:

Comes now the Petitioner in the above-stated petition for a writ of certiorari, and respectfully shows to this Honorable Court:

That, in the response and brief of the Respondent in opposition to the grant of said petition, there are vital errors of fact, which—though inadvertent—would, if left uncorrected, gravely prejudice the Petitioner's case, to wit: On *page 13* of such response and brief is the statement, "In view of the *facts set forth in the statement, supra,* there was more than sufficient *evidence* to sustain a finding that the taxpayer never intended to make a gift of the stock to his wife. • • • There was ample *evidence* from

which the Tax Court could conclude" in favor of the Respondent's contention as to a partnership. (Italics ours.) In this "Statement" (pp. 3-12), no purported " fact," adverse to the Petitioner, relied on by the Respondent, represents any "Evidence" in the record (pp. 102-197), and no page is cited from such "Evidence." But all of the alleged "facts" in the "Statement" are taken only from the findings and conclusions of the Tax Court Judge (pp. 34-78). This appears from every citation made in the rssponse (pp. 4-12). The correctness of all these adverse findings, as unauthorized by any substantial evidence, has been duly challenged by the Petitioner's Assignments of Error in this Court and in the Court of Appeals (Petition for Certiorari and Supporting Brief, pp. 3-13, 36; Petition for Review, R. 88-99). The correctness of the facts as stated there, and on pages 30-36 of the present Petition, with citations from the Record Evidence itself, has not been questioned.

On *page 3* of the response, it is stated: "This case arises from a *consolidated proceeding* before the Tax Court," from which separate petitions for review were taken, and a petition for certiorari by other Sewells was denied on February 25, 1946. For convenience, the evidence was taken at the same time, and the Tax Court Judge rendered a consolidated memorandum opinion and findings, but there was no legal consolidation. "Each of said cases was heard before the Tax Court separately;" and separate decisions were rendered (R. 103, 84). The facts as to dominion and control, including sales and pledges by Mrs. Sewell herself as donee after the alleged stock gifts, were wholly different; and in the other cases there were no issues as to partnership. Here, there was no sort of fact to indicate any express or implied condition attached to the gifts, or continued dominion by the donor over them, or contem-

poraneous or near-connected agreement as to any loan or use of proceeds. Such assertions as "*facts*" (instead of as contentions), in the Response, are negatived by the Record Evidence (Citations from Record, Petition for Certiorari and Brief, pages 31-36).

Among other erroneous statements of alleged "*facts*" both as to gift and as to partnership, on *page 4* of the Response, is the statement: "At the time of, or subsequent to the issuance of the certificate, she endorsed them (the stock certificates) in blank, some of the endorsements not having been made until the times when her shares were sold." Quotations from the Record to negative each erroneous statement by the Respondent we believe would be here out of place; but we feel compelled to do so as to any "endorsements," since such a statement—if correct—would render this only a "fact case," the decisions of the lower courts authorized by evidence, and this petition wholly lacking in merit.

The endorsements "were not made at the time (the accountant) prepared the new stock certificates." He "did not see her(the donee) indorse the certificates * * * didn't hand the certificates to her and ask her to indorse them" (R. 113, 123). The donee "didn't indorse these shares soon after they were transferred to (her); maybe one of them in the Fall following the gift * * * along about the time of the sale." She "sold them," and in 1936 she herself "entered into certain pledge contracts" with shares of the stock as security. "I (the donee) sold some of the stock myself; the other I pledged to borrow money on." The first sale by her was on December 29, 1934 (the gift on January 2, 1934); other sales by her in 1935, 1936, and 1937; and the written, recorded pledge contracts were executed by her on October 31 and December 18, 1936 (R. 155, 157; Doc. Ev., Exhs. 1, 2, 13, 22-26). Un-

der these supported, undisputed facts, with subsequent acts of the donee, the statement that "at the time of * * * the issuance of the certificates" (or subsequently) she "endorsed them" or some of them—with implications as to the donor's continued control—is inaccurate and does the Petitioner a grave injustice.

None of the facts in her petition and supporting brief, and none of the Reasons for Granting the Writ, there stated, have been challenged by the Respondent. The only reason urged for a denial, under the recent *Tower* and *Lusthaus* partnership decisions and inapplicable mere "fact" cases, is the erroneous or inaccurate (though inadvertent) statement, *as "facts,"* of matters which the Petitioner has challenged, and now again respectfully challenges, as wholly unsupported by the record.

WHEREFORE, the Petitioner respectfully moves that the above-stated vital errors of fact be corrected by the Respondent, or that such matters in the Respondent's "Statement" be not considered as *"facts"* in passing upon her petition.

O. C. HANCOCK,
CLIFFORD R. WHEELESS,
Counsel for Petitioner.